

Message Text

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PAGE 01 BRUSSE 10456 01 OF 03 301625Z
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TAGS: EGEN, EFIN, EEC, US
SUBJECT: BILATERAL US/EC CONSULTATIONS MAY 25-26
PART I: GENERAL ECONOMIC SITUATION

1. SUMMARY: US/EC CONSULTATIONS OPENED WITH REVIEW OF
GENERAL ECONOMIC SITUATION, FOCUSING ON APPROACHING
WESTERN ECONOMIC SUMMIT. THE TWO SIDES AGREED ON THE
NEED FOR COORDINATED INTERNATIONAL ACTION TO IMPROVE
UNSATISFACTORY GROWTH PROSPECTS. COMMISSION REPS
REVIEWED DEVELOPMENT OF COMMUNITY CONCERTED ACTION PROGRAM
AIMED AT BOOSTING PARTICULARLY WEAK EUROPEAN GROWTH OUT-
LOOK TOWARDS TARGET OF 4 1/2 PERCENT BY MID-1979. EC
SIDE ALSO HIGHLIGHTED DISPARITIES WITHIN COMMUNITY ON
INFLATION TRENDS AND EXTERNAL BALANCE, AND DISCUSSED IN
GENERAL TERMS POSSIBLE NEAR-TERM STEPS TO IMPROVE INTRA-
EUROPEAN EXCHANGE STABILITY. US APPLAUDED COMMISSION
EFFORTS IN GROWTH AREA, EXPRESSED SYMPATHY FOR EUROPEAN
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PAGE 02 BRUSSE 10456 01 OF 03 301625Z

QUEST FOR GREATER MONETARY COHESION AND SUPPORT FOR
ULTIMATE AIM OF ECONOMIC AND MONETARY UNION.

IN CONTEXT OF SUMMIT STRATEGY THE TWO SIDES EXCHANGED
SIMILAR VIEWS ON JAPAN AND RESOURCE TRANSFER TO LDC'S.

RESPONDING FAVORABLY TO US SUPPORT FOR OECD INITIATIVE

TO DEAL WITH GROWING GOVERNMENT MICROECONOMIC INTERVENTIONS ("POSITIVE ADJUSTMENT POLICIES"), EC SUGGESTED THAT EFFORT BE CENTERED IN GATT. END SUMMARY.

2. THE US/EC COMMISSION SEMI-ANNUAL BILATERAL CONSULTATIONS WERE HELD IN BRUSSELS MAY 25-26. THE US DELEGATION WAS HEADED BY UNDER SECRETARY COOPER, WHILE THE EC SIDE WAS HEADED BY COMMISSION VICE PRESIDENT WILHELM HAFERKAMP.

3. THREE PLENARY SESSIONS WERE HELD COVERING THE GENERAL ECONOMIC SITUATION AND SUMMIT STRATEGY, TRADE AND INDUSTRIAL POLICIES, NORTH/SOUTH ISSUES, AND ENERGY. A SEPARATE WORKING GROUP ALSO DISCUSSED STEEL AND TRADE MATTERS. THIS MESSAGE REPORTS ON DISCUSSIONS HELD ON THE GENERAL ECONOMIC SITUATION AND SUMMIT STRATEGY. SEPARATE MESSAGES WILL COVER REMAINING TOPICS.

4. VICE PRESIDENT HAFERKAMP SUGGESTED THAT DISCUSSIONS ON THE GENERAL ECONOMIC SITUATION BE FOCUSED ON PREPARATION FOR MAJOR UPCOMING INTERNATIONAL ECONOMIC MEETINGS -- THE OECD MINISTERIAL, THE EUROPEAN SUMMIT, AND THE WESTERN ECONOMIC SUMMIT.

5. EC DIRECTOR GENERAL MOSCA REVIEWED THE COMMISSION'S OUTLOOK ON THE ECONOMIC SITUATION. GROWTH PROSPECTS APPEARED INADEQUATE WITH 1979 GROWTH IN EUROPE ESTIMATED LIMITED OFFICIAL USE

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PAGE 03 BRUSSE 10456 01 OF 03 301625Z

AT UNDER 3 PERCENT, FOLLOWING 2.6 PERCENT IN 1978. THE COMMUNITY WAS CONVINCED OF THE NEED FOR A COORDINATED STRATEGY BOTH WORLDWIDE AND WITHIN THE EC. DISCUSSIONS WERE UNDERWAY WITHIN THE COMMUNITY AIMED AT "CONCERTED ACTION" WHICH WOULD BE DESIGNED TO RAISE EC ECONOMIC GROWTH TOWARDS THEIR TARGET OF 4 1/2 PERCENT BY MID-1979. A CONCERTED APPROACH WAS NECESSARY IN ORDER TO EASE THE CONSTRAINTS WHICH WERE NOW IMPEDING THE FREEDOM OF ACTION OF INDIVIDUAL MEMBER STATES. THE COMMISSION HAD ESTIMATED THAT WITH CONCERTED ACTION, FISCAL POLICY MULTIPLIERS WOULD BE RATHER HIGH -- ABOUT 2 -- AND THAT TOTAL MEASURES OF SOMEWHAT LESS THAN 1 PERCENT OF GNP MIGHT THEREFORE BE APPROPRIATE TO REACH THE COMMUNITY TARGET. THE CONTRIBUTIONS OF INDIVIDUAL MEMBER STATES HAD NOT YET BEEN DECIDED, BUT IT WAS HOPED THAT CONCRETE RECOMMENDATIONS WOULD BE MADE BY THE JUNE 19 FINANCE COUNCIL MEETING. THE EUROPEAN SUMMIT IN BREMEN COULD THEN ENDORSE THIS PROGRAM, PERMITTING THE EC TO MAKE AN EFFECTIVE CONTRIBUTION TO THE OUTCOME OF THE WESTERN ECONOMIC SUMMIT IN BONN.

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PAGE 01 BRUSSE 10456 02 OF 03 301632Z
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6. MOSCA EMPHASIZED THAT CONCERTED ACTION MUST AIM AT NONINFLATIONARY GROWTH, WITH THE COMMUNITY AIMING TO REDUCE THE INFLATION RATE IN 1979 TO ABOUT 7 PERCENT, AND TO REDUCE DIVERGENCES AMONG MEMBER STATES ON BOTH INFLATION TRENDS AND THE BALANCE OF PAYMENTS. HE CITED DIVERGENCES IN ESTIMATED RATES OF INFLATION FOR 1978 RANGING BETWEEN GERMANY, 3.3 PERCENT; THE NETHERLANDS AND BELGIUM, ABOUT 5 PERCENT; FRANCE AND THE UK, 8 TO 9 PERCENT; AND ITALY, ABOUT 13 PERCENT. ON THE EXTERNAL SIDE, THE COMMUNITY WAS MOVING INTO AN OVERALL SURPLUS IN 1978. GERMANY WOULD HAVE A SURPLUS OF ABOUT 3.7 BILLION DOLLARS, ITALY ABOUT 2 BILLION DOLLARS, THE NETHERLANDS ABOUT 1.4 BILLION DOLLARS, THE UK 1 BILLION DOLLARS, AND BELGIUM 0.4 BILLION DOLLARS. ON THE OTHER HAND, DEFICIT COUNTRIES WERE FRANCE (ABOUT 3 BILLION DOLLARS), DENMARK (1.2 BILLION DOLLARS), AND IRELAND (0.4 BILLION DOLLARS). MOSCA ALSO NOTED THE QUESTION OF THE APPROPRIATENESS OF AN OVERALL EC CURRENT ACCOUNT SURPLUS WHILE THE WORLD ECONOMY HAD NOT YET ADJUSTED TO THE INCREASE IN OIL PRICES.

7. MOSCA NOTED THAT, WITH THE BROAD AIM OF ACHIEVING
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PAGE 02 BRUSSE 10456 02 OF 03 301632Z

ECONOMIC AND MONETARY UNION (EMU) IN THE BACKGROUND,
EUROPEANS WERE CONCERNED TO IMPROVE THE STABILITY OF

EXCHANGE MARKETS. A MORE HARMONIOUS UNDERLYING ECONOMIC SITUATION IS OF COURSE THE NECESSARY CONDITION FOR MORE STABLE RATES. BUT CONVERSELY, THE EXAGGERATED BEHAVIOR OF EXCHANGE RATES MAY ALSO INCREASE THE DIFFICULTY OF ACHIEVING THE AIMS OF THE DEMAND MANAGEMENT POLICIES. THEREFORE, TOGETHER WITH MEASURES TO IMPROVE UNDERLYING ECONOMIC CONVERGENCE, SOME MEASURES ARE NOW SEEN APPROPRIATE IN THE EXCHANGE RATE FIELD. NO CONCLUSIONS HAVE YET BEEN REACHED BOTH BECAUSE OF THE INTRINSIC DIFFICULTY OF THE PROBLEM AND THE NEED FOR BROADER CONSULTATIONS, ESPECIALLY WITH THE UNITED STATES.

8. UNDER SECRETARY COOPER DESCRIBED THE SATISFACTORY RECENT US GROWTH PERFORMANCE. ASSUMING IMPLEMENTATION OF THE PRESIDENT'S TAX CUT PROGRAM, THE GROWTH RATE DURING 1979 OUGHT TO EASE OFF TO JUST BELOW 4 PERCENT, CONSISTENT WITH THE NEED TO GRADUALLY SLOW THE GROWTH RATE DOWN TO THE LONG-RUN SUSTAINABLE RATE OF ABOUT 3 1/2 PERCENT AS THE ECONOMY APPROACHED FULL EMPLOYMENT. AS FULL EMPLOYMENT APPROACHED, THE BALANCE OF CONCERN WAS APPROPRIATELY SHIFTING TO INFLATION. COOPER REVIEWED THE RECENTLY ANNOUNCED PROGRAM TO DEAL WITH THE INFLATIONARY THREAT AND SUMMED UP THE US CONTRIBUTION TO THE SUMMIT STRATEGY AS CONTINUING TO CONTRIBUTE TO WORLD ECONOMIC GROWTH AND RECOVERY, WITH INCREASED ATTENTION TO INFLATION, AND MEASURES ON ENERGY. COOPER SAID THE US SHARED FULLY THE COMMISSION'S VIEWS ON THE NEED FOR INCREASED GROWTH IN EUROPE AND STRONGLY APPLAUDED THE COMMISSION'S EFFORT TO ACHIEVE THIS.

9. ON THE MONETARY SIDE, COOPER REAFFIRMED US BELIEF THAT LIMITED OFFICIAL USE

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PAGE 03 BRUSSE 10456 02 OF 03 301632Z

IT WAS APPROPRIATE FOR INDUSTRIALIZED COUNTRIES TO CONTINUE TO RUN CURRENT ACCOUNT DEFICITS SO LONG AS OPEC SURPLUSES CONTINUED TO BE LARGE. HE NOTED THAT THE OPEC SURPLUS WAS PROJECTED TO DECLINE SHARPLY THIS YEAR, AND THEREFORE IT WAS NOT SURPRISING THAT EUROPE SHOULD BE EXPERIENCING A FAVORABLE SWING IN THEIR CURRENT ACCOUNT POSITION. NEVERTHELESS, THE US WOULD STILL LIKE TO SEE A BETTER BALANCE IN THE WORLD PAYMENTS SITUATION, WITH A SMALLER US DEFICIT AND A MUCH SMALLER JAPANESE SURPLUS. EUROPE SHOULD STILL AIM FOR A DEFICIT POSITION.

10. THE US SEES LESS SCOPE FOR USEFUL DIRECT MEASURES IN THE FOREIGN EXCHANGE MARKETS. WE CONTINUE TO PLACE PRIMARY EMPHASIS ON FUNDAMENTAL IMPROVEMENTS, PARTICULARLY REDUCING INFLATION DIVERGENCES, BUT RECOGNIZE ALSO THE NEED TO INTERVENE TO COUNTERACT EXCESSIVE PSYCHOLOGICAL MOVEMENTS. COOPER UNDERSTOOD THAT EUROPE FELT THE UNITED

STATES SHOULD DO MORE BUT HAD NOT HEARD ANY CONCRETE
FEASIBLE PROPOSALS. THERE WAS A RISK OF AGGRAVATING
EXCHANGE MARKET UNEASINESS IF THERE WERE CONTINUED TALK
ABOUT THE NEED TO TAKE DIRECT ACTION WHEN APPROPRIATE
INSTRUMENTS ARE IN FACT LACKING.

11. COOPER EXPRESSED INTEREST IN DETAILS ON EUROPEAN
MONETARY PLANS TO FOLLOW UP COPENHAGEN. SOME PRESS
INTERPRETATION OF THE COPENHAGEN MEETING HAD SUGGESTED
THAT EUROPEAN MOVES WERE ANTI-US OR ANTI-DOLLAR IN NATURE,
BUT THIS IS NOT THE US VIEW. THE US SUPPORTS EUROPEAN
OBJECTIVES FOR EMU AND FINDS EUROPEAN DISCUSSION OF NEAR-
TERM MEASURES WHOLESOME.

12. HAFERKAMP EXPRESSED GRATIFICATION FOR US UNDERSTANDING
AND STRONGLY CONFIRMED THAT EUROPEAN MONETARY INITIATIVES
WERE NOT AT ALL DIRECTED AGAINST THE US OR THE DOLLAR.
MOSCA SAID THAT DETAILS OF MONETARY INITIATIVES WERE STILL

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PAGE 01 BRUSSE 10456 03 OF 03 301741Z
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FAR FROM WORKED OUT, BUT MIGHT INVOLVE MODEST STEPS TOWARDS
MORE STABLE RELATIONSHIPS BETWEEN SNAKE AND NON-SNAKE
MEMBER STATES AS A TRANSITIONAL STEP LEADING LATER TO MORE
STRINGENT ARRANGEMENTS. INCREASED EXCHANGE RATE
COORDINATION WOULD NEED TO BE COMBINED WITH MORE
CONDITIONALITY AND DISCIPLINE OVER INTERNAL MEMBER STATE
POLICIES.

13. MOSCA FELT GREATER INTRA-EUROPEAN EXCHANGE RATE

STABILITY COULD MAKE A CONTRIBUTION TO GLOBAL STABILITY.
IT WAS IMPORTANT THAT THE US SUPPORT THE GOAL OF EMU.
THE APPROPRIATE US CONTRIBUTION IN THE MONETARY AREA IS TO
CONTINUE ITS INCREASED EFFORTS TO SMOOTH OUT ERRATIC
EXCHANGE RATE MOVEMENTS.

14. THE TWO SIDES EXCHANGED VIEWS ON THE ROLE OF JAPAN IN
SUMMIT STRATEGY. COOPER NOTED THAT IT SEEMED UNLIKELY
THAT JAPAN WOULD REACH ITS 7 PERCENT GROWTH TARGET WITHOUT
FURTHER MEASURES. HE UNDERSTOOD THAT PREPARATION FOR
ADDITIONAL EXPANSIONARY POLICY WAS UNDERWAY, ALTHOUGH
NECESSARY POLITICAL DECISIONS HAD NOT BEEN TAKEN. THE
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PAGE 02 BRUSSE 10456 03 OF 03 301741Z

OBJECTIVE OF A 6 BILLION DOLLAR CURRENT ACCOUNT SURPLUS
OBVIOUSLY WAS OUT OF REACH AND JAPAN WAS LOOKING TO STOP-
GAP METHODS TO EASE PRESSURE WHILE ADJUSTMENT IS TAKING
PLACE, INCLUDING STOCKPILING OF OIL, NON-FERROUS METALS,
URANIUM AND AIRCRAFT. THE EC SHARED THESE VIEWS AND
EMPHASIZED THE NEED FOR JAPAN TO TAKE CONCRETE MEASURES,
PARTICULARLY TO REDUCE IMPORT BARRIERS. IF THERE IS NO
IMPROVEMENT, MEASURES AGAINST JAPANESE EXPORTS BECOME A
POSSIBILITY WHICH THE COMMISSION WANTS TO AVOID.

15. IN THE CONTEXT OF GROWTH STRATEGY, THE TWO SIDES ALSO
EXCHANGED VIEWS ON NORTH/SOUTH ISSUES. THE COMMISSION
ARGUED FOR RESOURCE TRANSFER TO LDC'S AS A TOOL OF DEMAND
MANAGEMENT POLICY. COOPER SAID IT WOULD BE DIFFICULT TO
FIND APPROPRIATE MECHANISMS ACCEPTABLE TO BOTH SIDES
WHICH COULD ALSO PROVIDE THE NECESSARY DISCIPLINE OVER
LDC POLICIES. IN ADDITION TO EXISTING MECHANISMS, OTHER
MECHANISMS MIGHT BE EXPLORED, SUCH AS MEANS TO FINANCE OIL
EXPLORATION IN LDC'S AND R & D EXPENDITURES ON NATURAL
FIBERS.

16. COOPER CALLED ATTENTION TO THE PROBLEM OF INCREASING
GOVERNMENT MICROECONOMIC INVOLVEMENT -- "THE NEW PROTEC-
TIONISM". THE DANGER WAS THAT THESE MEASURES MIGHT BECOME
PERMANENT, THUS UNDERMINING THE "SOCIAL MARKET ECONOMY"
WHICH HAS PROVED SO EFFICIENT. COOPER URGED SUPPORT FOR
THE OECD EFFORT ("POSITIVE ADJUSTMENT POLICIES") TO TAKE
STOCK OF THESE MEASURES AND TRY TO INSURE THAT THEY DO NOT
BECOME PERMANENT FEATURES. HAFERKAMP AGREED WITH THE
DESIRABILITY OF DEALING WITH THIS PROBLEM. THERE WAS A
NEED TO TRANSFER THIS CORRECT IDEA INTO CONCRETE FORM, AND
INTO AN OPERATIONAL FRAMEWORK VIA EXISTING ORGANIZATIONS,
IN PARTICULAR THE GATT. GATT NEGOTIATIONS SHOULD AIM AT
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PAGE 03 BRUSSE 10456 03 OF 03 301741Z

STRENGTHENED RULES AND PROCEDURES TO DEAL WITH THIS
PROBLEM. HINTON

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